# SUPREME COURT OF THE UNITED STATES

## OCTOBER TERM, 1940

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# No. 854

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PHILLIPS PETROLEUM COMPANY, A CORPORATION,
*Petitioner and Appellant below,*

*vs.*

MRS. VOLNEY W. TAYLOR, VOLNEY W. TAYLOR, J. L. GRAY AND SABINE ROYALTY CORPORATION,
*Respondents and Appellees below.*

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## BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

### I.

### Opinions of Court Below.

The original opinion in the Circuit Court of Appeals for the Fifth Circuit is reported in 115 F. (2d) at page 726 and the opinion on petition for rehearing appears in 116 F. (2d) at page 994.

### II.

### Jurisdiction.

1. The date of the decree to be reviewed is November 29, 1940 (R. 263). Petition for rehearing was denied on January 14, 1941 (R. 291).

2. The statutory provision which is believed to sustain the jurisdiction of this Court is Act of Congress Mar. 3, 1891, c. 517, § 6, 26 Stat. 828; Mar. 3, 1911, c. 231, § 240, 36 Stat. 1157; Feb. 13, 1925, c. 229, § 1, 43 Stat. 938; Judicial Code, Sec. 240; U. S. C., Title 28, Sec. 347.

3. This is a civil action in the United States Circuit Court of Appeals for the Fifth Circuit and therefore it is competent for this Court, upon the petition of any party thereto, to require by certiorari, either before or after a judgment or decree by said Circuit Court of Appeals, that the cause be certified to this Court for determination by it with the same power and authority, and with like effect, as if the cause had been brought to this Court by unrestricted writ of error or appeal.

4. The cases believed to sustain said jurisdiction are as follows:

*American Construction Company* v. *Jacksonville, T. & K. W. R. Company,* 148 U. S. 372;

*United States* v. *The Three Friends,* 166 U. S. 1; and

*Forsyth* v. *City of Hammond, et al.,* 166 U. S. 506.

## III.

### Statement of the Case.

Inasmuch as a summary of the case has been set forth in the preceding petition under paragraph I, that statement hereby is adopted and made a part of this brief.

## IV.

### Specification of Errors.

1. The United States Circuit Court of Appeals for the Fifth Circuit erred in holding that owners of oil royalty interests reserved and created by an *oil and gas lease* have

such a common and undivided interest with the owner of an oil payment *created by and excepted under a subsequent assignment* of said oil and gas lease that they may aggregate all of their interests to attain the required jurisdictional amount in a suit for damages against the oil and gas lessee for failure to protect the leased premises from drainage.

2. The said Circuit Court of Appeals erred in holding that the assignor of an oil and gas lease, by excepting an interest in the oil, gas and other minerals to be produced thereunder, is entitled to the benefit of an implied covenant on the part of his assignee, to protect the leased premises against drainage.

3. The said Circuit Court of Appeals erred in assuming, contrary to the record, that the $18,750.00 oil payment excepted by respondent Gray in his assignment of the oil and gas lease in question to petitioner constituted the sole consideration for such assignment.

## V.

## ARGUMENT.

### Summary of the Argument.

Point A. The United States District Court had no jurisdiction of the claims of plaintiffs-respondents Mrs. Volney W. Taylor and Sabine Royalty Corporation. Their claims as shown by their complaint (R. 6-8) are for sums of only $1,390.63 each. Jurisdiction of the federal court was invoked on the ground of diversity of citizenship. Their claims cannot be aggregated with the claim of respondent Gray, whose claim exceeded the sum of $3,000.00. The Circuit Court of Appeals erroneously held that the several plaintiffs united "to enforce a single title or right in which they have a common and undivided interest against the

defendant * * *. The interest of each of the plaintiffs was derived from the same instrument, the assigned mineral lease, and the liability of the defendant too was based solely upon it." The claims of respondents Mrs. Volney W. Taylor and Sabine Royalty Corporation are based upon the oil and gas lease dated August 22, 1934, (R. 27-34) while the claim of respondent Gray is based upon the assignment of that lease, wherein an oil payment was reserved to Gray, dated October 22, 1934, (R. 160-164). Prior to the making of the assignment respondent Gray was the sole obligee to the respondents Mrs. Volney W. Taylor, Sabine Royalty Corporation and other owners of interests in the ⅛ royalty reserved by the lease. Obviously, therefore, the claims of Mrs. Volney W. Taylor and Sabine Royalty Corporation were separate and distinct from the claim of Gray and arose out of separate and distinct instruments. *Simms Oil Company* v. *Colquitt* (1926-Tex. Civ. A.) 289 S. W. 98 (reversed on other grounds in *Simms Oil Company* v. *Colquitt* (1928 Tex. Com. A.), 2 S. W. (2d) 421); *Greenwood & Tyrrell* v. *Helm* (1924-Tex. Civ. A.) 264 S. W. 221; *Henderson Company* v. *Murphy,* 189 Ark. 87, 70 S. W. (2d) 1036; *Kile* v. *Amerada Petroleum Corporation,* 118 Okl. 176, 247 Pac. 681.

The claims were not joint. *Clark* v. *Gray,* 306 U. S. 583 (1939); *Pinel* v. *Pinel,* 240 U. S. 594.

Point B. The respondent Gray has no right of action against the petitioner for its failure to protect the leased premises against drainage. His interest is in the nature of a limited overriding royalty, created by the written instrument under which the oil and gas lease was assigned to petitioner (R. 160-164). That interest was payable out of ¼ of ⅞ (or ¼ of the lessee's portion) of the first oil and gas *if, as and when produced,* and the decisions are uniform in holding that no implied covenant to develop or to protect the property from drainage exists in favor of the owner of an oil payment or overriding royalty. *Greenwood*

*& Tyrrel* v. *Helm* (Tex. Civ. A. 1924) 264 S. W. 221; *Owens* v. *O'Donohoe,* 280 S. W. 842 (Tex. Civ. A. 1926); *Simms Oil Company* v. *Colquitt* (Tex. Com. A.-1927) 2 S. W. (2d) 421; *Matthews* v. *Ramsey-Lloyd Oil Company,* 121 Kans. 75, 245 Pac. 1064; *Kile* v. *Amerada Petroleum Corporation,* 118 Okl. 176, 247 Pac. 681; *Henderson Company* v. *Murphy,* 189 Ark. 87, 70 S. W. (2d) 1036.

The case of *American Sulphur Royalty Company* v. *Freeport Sulphur Company,* 276 S. W. 448, cited by the Circuit Court of Appeals is not in point inasmuch as that case involved the rights of the assignees of the lessor as against the assignees of the lessee. There was no overriding royalty or oil payment involved.

The above applicable Texas cases are binding upon the federal courts. *Erie Railway Company* v. *Tompkins,* 304 U. S. 64.

Point C. There is no evidence in the record indicating or tending to indicate that the sole consideration for the assignment of the oil and gas lease in question from respondent Gray to petitioner was the oil payment in the sum of $18,750.00 excepted by said assignment. The record clearly reflects a cash consideration and strongly indicates that such consideration was between $18,500.00 and $19,000.00. Insofar as the decision of the Circuit Court of Appeals is predicated upon the finding and assumption that said oil payment constituted the sole consideration for the assignment, it is erroneous.

**Point A.**

**The District Court had no jurisdiction of claims of respondents Mrs. Volney W. Taylor and Sabine Royalty Corporation.**

The complaint reflects that the oil drained and to be drained in the future from the leased premises by reason of production on adjacent lands would not exceed in value

the sum of $89,000.00 (R. 6-8). Of that sum, respondent Mrs. Volney W. Taylor and Sabine Royalty Corporation would be entitled to one sixty-fourth (1/64) each, or a maximum of $1,390.63. It is admitted that respondent Gray's claim exceeds the jurisdictional amount of $3,000.00. The question presented, therefore, is whether respondents Taylor and Sabine Royalty Corporation, owners of royalty interests under the oil and gas lease of August 22, 1934, having claims aggregating less than $3,000.00, may sue in the federal court on the ground of diversity of citizenship, by joining with respondent Gray whose claim exceeds the jurisdictional amount but arises under a separate instrument entirely different in character, *i.e.* the assignment of oil and gas lease bearing date of October 25, 1934.

In holding that the District Court had jurisdiction, the Circuit Court of Appeals said:

> "We think that this case involves several plaintiffs uniting to enforce a single title or right in which they have a common and undivided interest against the defendant. Such interests may be aggregated to make up the jurisdictional amount.[1] The interest of each of the plaintiffs was derived from the same instrument, the assigned mineral lease, and the liability of the defendant, too, was based solely upon it. The uncaptured produce from the mineral lease, recoverable only through the implied covenant, constituted the sole interest of all the plaintiffs; and the concern of the defendant in this suit was not to avoid any separate demand of the plaintiffs, but to escape the liability common to all. The demand was for a lump sum. The appellant was interested in the amount of that sum, and not the division to be made of it between the opposing parties.[2]

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[1] *Clay* v. *Field*, 138 U. S. 464; *Pinel* v. *Pinel*, 240 U. S. 594; Dobie on Federal Procedure, pp. 158, 159; Williams' Federal Practice, pp. 123-128.

[2] *Davies* v. *Corbin*, 112 U. S. 36.

> "There is no real difference between the case at bar and the leading case of Troy Bank *v.* Whitehead, 222 U. S. 39, which was a suit by two plaintiffs to enforce a vendor's lien. Each had bought one of two purchase-money notes in which a purchase-money lien had been retained." (R. 261.)

Petitioner respectfully submits this is not a case of "plaintiffs uniting to enforce a single title or right"; that the interest of each of the plaintiffs *was not* derived from the same instrument—the oil and gas lease; that the liability of defendant *was not* common to all of the plaintiffs; and that the case of *Troy Bank* v. *Whitehead is not* in point.

Directly in point, however, is the case of *Clark* v. *Gray*, 306 U. S. 583 (1939), wherein Mr. Justice Stone states that it is the duty of the appellate court to inquire into the jurisdiction of the lower courts *sua sponte*. The facts in that case are not distinguishable from those in the case at bar. Numerous persons joined in a suit against California officials to enjoin the enforcement of the California Caravan Act of 1937 levying a tax of $15.00 for each automobile driven into the state for sale. Finding that only one of the several parties bringing the suit would transport a sufficient number of automobiles into the state during the period of the litigation to incur a total tax liability of $3,000.00 or more, the court dismissed the action as to all other parties. It was held that the fact the complaint alleged the amount to exceed $3,000.00 and the fact that the defendant withdrew its motion challenging the jurisdiction of the court did not relieve the court of the duty to dismiss the action as to those parties shown by the face of the bill to have no joint or common interest or title in the subject matter of the suit and whose claims, individually, did not exceed $3,000.00. It was stated that no joint or common interest in the subject matter of the suit was established.

That is significant when it is considered that all of the parties were affected alike by a single statute enacted by the state.

In the instant case, any claim the respondent Gray may have is not predicated on the oil and gas lease, but arises out of the assignment thereof to petitioner. It is conceded that all holders of interests in the ⅛ royalty reserved in the lease have a common claim for violation of the implied covenants of the instrument. Respondents Taylor and Sabine Royalty Corporation undoubtedly could have prosecuted this action in federal court had their claims aggregated more tha $3,000.00. Respondent Gray, on the other hand, acquired any right of action he may have by virtue of the assignment executed two months after the execution and delivery of the oil and gas lease. *Prior to that time he was the sole obligee to the owners of the royalty interests under the lease.*

In *Simms Oil Company* v. *Colquitt* (1926), 289 S. W. 98, the Court of Civil Appeals of Texas, in holding that an assignment of an oil and gas lease in consideration of $7,000.00 cash and $7,000.00 payable out of ½ of ⅞ of the net oil produced obligated the assignee to drill, said:

> "It is insisted, however, that as Colquitt had the right under the original lease from Owens and wife to postpone drilling to the end of the lease by the payment of a specified rental, appellant, as his assignee, acquired the same option. We cannot assent to this proposition. *The original lease from Owens and wife to Colquitt and Graves, and the assignment from Colquitt to appellant, are distinct contracts. We are now dealing with the terms of the latter,*[3] which by agreement of the parties changed the option to drill, as contained in the original lease, to an obligation to drill within a reasonable time.

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[3] All italics in quotations are supplied.

> *"Colquitt, in the assignment of this lease, had the right to exact drilling terms more onerous than those contained in the original lease, and when agreed to by appellant, as we find by implication they were, the milder terms of the lease, so far as concerned appellee, were superseded."*

Although it reversed the holding of the lower court (*Simms Oil Co.* v. *Colquitt*, 2 S. W. (2d) 421), the Supreme Court of Texas did not take exception to the statement that the rights of the parties were governed by the assignment and that the assignment and lease were distinct contracts. That was recognized as true, but the Supreme Court held that the assignment, interpreted in the light of the terms in the lease which it assigned, did not obligate the assignee to drill. The court said:

> "The defendant in error contends that, *under the implied terms of said assignment*, the oil company became obligated to him to make reasonable efforts to produce the oil from which his claim is payable, * * *.
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> "* * * By the authority of that decision, we are constrained to hold that, *under the assignment in question*, the oil company did not become unconditionally obligated to the defendant in error to make efforts to produce oil from the leased premises."

In *Greenwood & Tyrell* vs. *Helm* (1924), 264 S. W. 221, the Texas Court of Civil Appeals, in holding that no obligation existed to drill wells under the terms of an assignment of an oil and gas lease for a consideration of $16,000.00 in cash and $3,200.00 payable out of the first net oil produced, after determining that no obligation to drill existed under the terms of the lease, said:

> "So, if appellants assumed the unconditional obligation to drill, *such obligation must arise alone out of the contract of assignment* since appellants by accepting the original lease simply stepped into the shoes of the

original lessee, whose liabilities thereunder passed to the successive assignees, which include appellee as well as appellants. Thornton Oil & Gas, Sec. 230, *et seq. We will consider the assignment then, to ascertain if appellants' obligation to drill was enlarged thereby.*"

Considering the intention of the parties as expressed in the assignment, the court held that the assignee was within its rights in releasing the lease without drilling.

Holding that there was no implied covenant to protect property from drainage under circumstances similar to those prevailing in the case at bar, the Supreme Court of Arkansas in *Henderson Company* vs. *Murphy*, 189 Ark. 87, 70 S. W.(2d) 1036, said:

> "Appellee's rights must depend, as said in Murdock *v.* Sure Oil Corporation, 171 Ark. 61, 283 S. W. 4, 6 '*On the protection paragraph of the written assignment,*' and there being no right, such as is here asserted, his action must fail."

In *Kile* v. *Amerada Petroleum Corporation*, 118 Okl. 176, 247 Pac. 681, a case involving facts almost identical to those in the case at bar, the court said:

> "It is clear to our minds that the right of the plaintiff to require the drilling of offset wells is dependent upon an obligation assumed by the defendant *in the contract of assignment* to drill a well upon the property covered by plaintiff's lease. * * *
>
> "But an examination of the *contract of assignment* in the instant case fails to disclose that the defendant expressly covenanted to drill or prospect for oil and gas upon the premises covered by the lease assigned to it. It is contended, however, that this obligation *must be implied from the obligation expressly made in the assignment* to pay or deliver one-eighth of the oil and gas and casinghead gas produced. However, we do not understand, even in an oil and gas lease, that the covenant or obligation of the lessee to drill or develop the premises for oil and gas can be implied where

there is no express covenant or obligation contained in the lease itself."

The foregoing authorities are cited in support of the contention that the obligation of the petitioner to respondent Gray, if any such obligation exists, arises out of the contract of assignment rather than out of the oil and gas lease whereas the obligation of petitioner to the other respondents arises out of the oil and gas lease. The claims are separate and distinct.

Assuming that respondent Gray is entitled to the benefit of an implied covenant to protect the leased premises from drainage, his rights not only arise under a different instrument than those under which the other respondents claim, but his rights are measured by a different standard. As against the claims of the respondents Taylor and Sabine Royalty Corporation, owners of interests in the landowners' 1/8 royalty, the obligation of petitioner was to drill offset wells if a reasonably prudent operator would have concluded that production could have been obtained in such volume that *7/8* thereof would pay the cost of drilling, equipping and operating the wells, plus a reasonable profit. As against the claim of respondent Gray, however, the obligation of petitioner at most was to drill offset wells if a reasonably prudent operator would have concluded that production could have been attained in such volume that *21/32* thereof would pay such costs plus a reasonable profit. 2 Summers Oil & Gas (Perm. Ed.) 117; *Texas Pacific Coal & Oil Company* v. *Barker,* 117 Texas 418, 6 S. W. (2d) 1031, 1036. Thus it may be seen that respondents Taylor and Sabine Royalty Corporation might have prevailed while the claim of respondent Gray, assuming that such a claim existed, could properly have been denied.

The case of *Pinel* v. *Pinel,* 240 U. S. 594, is directly in point. Charles T. Pinel died testate leaving certain real

estate. His will did not mention any of his children, two of whom joined in a suit to establish their interests in his property. The jurisdictional questions certified to the Supreme Court were, (1) whether the amount in controversy was sufficient to give the court jurisdiction and (2) whether the parties were collusively joined. In affirming the decree of the district court dismissing the bill for want of jurisdiction, the Supreme Court, speaking through Mr. Justice Pitney, said:

> "The settled rule is that when two or more plaintiffs having separate and distinct demands unite in a single suit, it is essential that the demand of each be of the requisite jurisdictional amount; but when several plaintiffs unite to enforce a single title or right in which they have a common and undivided interest, it is enough if their interests collectively equal the jurisdictional amount. Clay *v.* Field, 138 U. S. 464, 479; Troy Bank *v.* G. A. Whitehead & Co., 222 U. S. 39.
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> "*This case comes within the former class, since the title of each complainant is separate and distinct from that of the other; it being evident that the testator's omission to provide for one of his children by will, based upon mistake or accident, is independent of the question whether a like mistake was made with respect to another child.*" (Emphasis supplied.)

It is not sufficient that the obligations to all of the respondents might have been discharged by the same act—that is, by drilling offset wells. To be considered collectively for jurisdictional purposes, the claims must be such that they may be measured and determined by the same standards.

It has been observed that the case of *Troy Bank* v. *Whitehead*, 222 U. S. 39, was a joint suit by two plaintiffs, each owning and holding one of two purchase-money notes in which a purchase-money lien had been retained, to enforce a vendor's lien. The case was cited by the Circuit Court

of Appeals in its first opinion to support its conclusion. Petitioner respectfully submits the decision is not in point. The court said:

> "The present suit is of the latter class. [Several plaintiffs uniting to enforce a single title or right in which they have common and undivided interests.] Its controlling object—that which makes it cognizable in equity—is the enforcement of the vendor's lien, which is a single thing or entity in which the plaintiffs have a common and undivided interest, *and which neither can enforce in the absence of the other.* Thus, while their claims under the notes were separate and distinct, *their claim under the vendor's lien was single and undivided,* and the lien was sought to be enforced as a common security for the payment of both notes."

In the instant case, the respondents were not seeking to enforce a lien; no property is involved in the action and it was not at all essential that the respondents file a joint suit. As a matter of fact, some of the owners of interests in the 1/8 landowners' royalty and some of the owners of interests in the oil payment are not parties to this action.

**Point B.**

**Under local decisions, respondent Gray has no right of action for failure of petitioner to protect the leased property from drainage.**

Simply stated, the question is, Does the benefit of an implied covenant to protect the leased premises against drainage by drilling offset wells extend to the assignor of a mineral lease who retains an interest in the oil and gas to be produced thereunder?

Although the Circuit Court of Appeals has cited the case of *American Sulphur Royalty Company* v. *Freeport Sulphur Company,* 276 S. W. 448, 6 S. W. (2d) 1039, (R. 259) in support of its decision herein, it respectfully is submitted

that said case is not in point and that the principles of law there announced, when applied to the facts in the case at bar, compel a contrary decision. The exact question with which the court is confronted herein has not been determined by the appellate courts of Texas, but those courts have considered the question as to whether an assignment of an oil and gas lease containing a provision for payment of a part of the consideration out of oil implies a covenant to develop. It has been held consistently that no such implied obligation arises. *Greenwood & Tyrrell* v. *Helm* (Tex. Civ. App. 1924), 264 S. W. 221; *Owens* v. *O'Donohoe,* 280 S. W. 842; *Simms Oil Company* v. *Colquitt* (Tex. Com. App. 1927), 2 S. W. (2d) 421.

On first impression it may be thought that the situation involved in the case at bar is distinguishable from that involved in the foregoing Texas cases, but it respectfully is submitted that there is no difference in principle. The oil out of which respondent Gray was to receive his payment might be drained from the land and be lost to him forever. He would suffer the same loss, however, if drilling were deferred and the lease permitted to expire. The Texas cases cited recognize such right on the part of the lessee to defer drilling. Needless to say, upon expiration of the lease the rights of the oil payment holder would be extinguished. The theory then must be that where an assignment reserving an overriding royalty is made with no express provision for development, the parties must contemplate that the assignor will receive his overriding royalty only in the event the assignee, in the exercise of his own good judgment, shall deem it advisable to develop the leased premises.

The Federal courts, both the trial court and the Circuit Court of Appeals for the Fifth Circuit, were bound to apply the Texas law. *Erie Railroad Company* v. *Harry J. Tompkins,* 304 U. S. 64. And while the Texas decisions are not squarely in point, they are analogous to such an extent there

can be no doubt the courts of that State would hold that no implied covenant to drill would exist under the facts in the instant case.

In at least two States in the mid-continent field, however, the exact question has been considered by courts of last resort. The Supreme Court of a third State, Kansas, held in *Matthews* v. *Ramsey-Lloyd Oil Company,* 121 Kan. 75, 245 P. 1064, that no covenant to develop is implied by an assignment of the nature of that in the case at bar. The case, however, did not involve a drainage question.

*Kile* v. *Amerada Petroleum Corporation,* 118 Okl. 176, 247 Pac. 681, is directly in point. In holding that the assignor of an oil and gas lease who had reserved an overriding royalty was not entitled to the benefit of an implied covenant on the part of the lessee to protect the leased premises from drainage by offset wells, the Supreme Court of Oklahoma found that the rights of the parties must be governed entirely by the provisions of the contract of assignment and that since said contract contained no specific obligation to either drill or protect the land from drainage, none would be implied. The court said:

> "*There must be some express covenant entered into upon which to base the implied obligation,* and, if the court should undertake to supply the primary framework of the agreement which the parties themselves have omitted, it would constitute an invasion of the domain of private contract reserved to individuals under the law.
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> "It is usual in leasing contracts, and other instruments in which the development and operation of land for oil and gas is contemplated, to impose an obligation upon the lessee to drill a well within a certain time, or to purchase the right to delay the commencement of such well for a definite time for a given consideration, but the primary purpose in all such contracts is to bring about the development of the premises for oil and

gas within a given time or within such time as drilling may be delayed upon payment of the agreed consideration therefor. There is an entire absence of such conditions and stipulations in the contract of assignment involved in the instant case.

"To hold that these fundamental provisions in leasing contracts are to be implied in the contract of assignment involved here, and then hold that plaintiff's right to recover can be based upon these implied provisions, coupled with the further implied covenant to drill offset wells, would be to stretch the rule beyond legitimate bounds. *No court to our knowledge has ever gone so far.* If, as contended by plaintiff, the assignment contract in question should be regarded as a sub-lease the same rule would apply. In either case *there is no express agreement contained in the contract which could form the basis of relief for the breach of an implied obligation to drill offset wells.*"

And in *Henderson Company* vs. *Murphy,* 189 Ark. 87, 70 S. W. (2d) 1036, the Supreme Court of Arkansas considered a case in which the assignor of an oil and gas lease had reserved an oil payment and sought damages against his assignee, the lessee, for failure to protect the leased premises against drainage by wells on adjacent land. The assignor-plaintiff obtained a verdict for $17,592.50 in the trial court. In reversing the case, the Arkansas court said:

"For a reversal of this judgment appellant makes a number of contentions. *First, that it had no obligation as to appellee to drill any wells on said lease, either to develop it, to protect it from drainage by offset wells, or to operate any of the wells that were drilled upon it. We think this contention is sound.* Appellee is neither a lessee nor an assignee of the lease. He is simply a purchaser from assignees of the leases of an interest in an overriding royalty or oil payment to become due and payable only if and when a sufficient quantity of oil were produced to pay out of the first one-half thereof his and prior obligations. The written instrument passing title

to him of oil payments from Gardner provides: 'Do hereby bargain, sell, transfer, assign, set over and deliver unto P. E. Murphy all my rights, title and interest in and to $12,000, Twelve Thousand Dollars of the consideration payable out of oil under the terms of a certain assignment executed by me to W. D. Ball,' etc. There was no assignment or sale of an interest in the lease. *Appellee's rights must depend, as said in Murdock* v. *Sure Oil Corporation,* 171 Ark. 61, 283 S. W. 4, 6, *'on the protection paragraph of the written assignment,' and there being no right, such as is here asserted, his action must fail. Kile* v. *Amerada Petroleum Corporation,* 118 Okl. 176, 247 P. 681; *Matthews* v. *Ramsey-Lloyd Oil Co.,* 121 Kan. 75, 245 P. 1064; *Simms Oil Co.* v. *Colquitt* (Tex. Civ. App.) 289 S. W. 98.

"This court is committed to the rule that, where a portion of the consideration for an oil and gas lease is payable out of the oil produced, if no oil is produced, then there is no payment due. As we said in *Gilbert* v. *Patterson,* 174 Ark. 61, 295 S. W. 386, 387: 'And the obligation, we think, was to pay out of the first oil produced and, if no oil was produced, there would be no obligation to pay.' See, also, *Hirsch* v. *Cadrin & Staten,* 178 Ark. 209, 10 S. W. (2d) 2."

It has been stated that the case of *American Sulphur Royalty Company* vs. *Freeport Sulphur Company, supra,* cited by the Circuit Court of Appeals in support of its decision herein, is not in point. The facts were that one Simms deeded the land in fee to one Swenson pursuant to a contract of sale reserving a stipulated royalty to Simms. Under the contract, the grantee was required to erect a sulphur plant upon the lands conveyed and commence operations in said plant within a designated time. Freeport Sulphur Company succeeded to the interest of Swenson. The royalty rights of Simms became vested in American Sulphur Royalty Company. *No additional royalties were provided* by any of the transfers and the litigation involved the rights of the royalty company as assignor of Simms and

the liability of the sulphur company as assignee of Swenson. The question, therefore, was whether, under the contract between Simms and Swenson, an implied covenant existed to fully and diligently develop the property. That is not the question in the case at bar. It is admitted that, under proper circumstances, an obligation is owing by the lessee, the petitioner in this case, to the lessor, the respondents Taylor and Sabine Royalty Corporation in this case, to protect the premises against drainage. And it is admitted, further, that such implied obligation extends to the assignees of those parties.

It has been stated, also, that the principles announced in the sulphur company case, when applied to the facts in the instant case, compel the conclusion that no implied covenant to protect against drainage existed as to respondent Gray. Thus, the court said:

> "The court cannot make contracts for parties, and can declare implied covenants to exist only when there is a satisfactory basis in the express contracts of the parties which makes it necessary to imply certain duties and obligations in order to effect the purposes of the parties in the contracts made. Before a covenant will be implied in the express terms of a contract, and in some cases in view of the customs and practices of the business to which the contract relates, it must appear therefrom that it was so clearly in the contemplation of the parties as that they deemed it unnecessary to express it, and therefore omitted to do so, or that it is necessary to imply such covenant in order to give effect to and effectuate the purpose of the contract as a whole."

And in treating the royalty provisions of the contract and conveyance, the Texas court observed:

> "* * * they were not *reservations* of an interest in the property, nor a retention of title to a part.

" 'Where a reservation in a deed cannot be construed as an exception, as where the thing reserved is not a part of that previously granted, it will be construed as an implied covenant on the part of the grantee.' 15 C. J., p. 1217.

"That the rule of implied covenants has had a special development as applied to the ordinary oil and gas lease does not make its proper application inappropriate to the mining of solid minerals in land acquired under fee-simple title, where the terms of the contract of sale make its application necessary to effectuate the purposes fairly evident in the writing. It really is a matter of interpreting the writings of the parties and ascertaining their intentions therefrom."

The Court then held:

"* * * It is our conclusion that this provision that a complete plant of one unit should be erected and put in operation does carry a very necessary implication for continued operation of said plant for the purposes of the contract regarding royalties to be paid to the royalty company. *The parties having contracted for development,* an implied covenant exists for diligent operation for the best advantage and benefit of both."

Applying those rules to the facts in the case at bar, it must be found that respondent Gray's oil payment is an *exception* and that the implication of a covenant on the part of the grantee, the petitioner, is improper. Reference to the assignment in question (R. 160) reveals that respondent Gray "hereby *excepts from said assignment* one-fourth (1/4) of seven-eighths (7/8) of the first oil produced and saved * * *."

Attention, also, is directed to the fact that in the sulphur case the court predicated the implied covenant to develop with reasonable diligence upon the express obligation to construct and operate a plant. In the assignment involved in the instant case, there was no express covenant to de-

velop the premises, to protect the premises against drainage or to do anything else other than pay respondent Gray the sum of $18,750.00 out of 1/4 of 7/8 of the first oil produced and saved and 1/4 of 7/8 of the net proceeds received at the well for gas marketed if, as and when such minerals were produced.

Insofar as the claim of respondent Gray is concerned, petitioner respectfully submits that the decision of the trial court and that of the Circuit Court of Appeals for the Fifth Circuit will have a very far-reaching effect; that said decision is in conflict with applicable local decisions; that it stands alone in the views expressed and conclusions reached and that the question is of such vital importance to the oil industry that this Court unquestionably is warranted in exercising its supervisory powers by reviewing the case.

**Point C.**

**The Circuit Court of Appeals for the Fifth Circuit was not justified in finding that the oil payment excepted by respondent Gray constituted the sole consideration for the assignment of the oil and gas lease to petitioner.**

It seems that little need be said in support of this point. The matter is mentioned merely for the reason that the Circuit Court of Appeals, in its opinion on the petition for rehearing, seems to have been influenced to such a great extent by the erroneous belief that the oil payment was the only consideration moving from petitioner to respondent Gray for the conveyance of the leasehold estate. Following are excerpts from the opinion:

> "Appellees Taylor and others executed an oil and gas lease to appellee Gray. Gray assigned the lease to appellant, retaining *as his sole consideration* (emphasis supplied), an overriding royalty, payable out of the first oil and gas produced. Personal property and equipment owned by Gray were included in the assignment.

The assignee exercised his rights under the assignment, and drilled some producing wells. (R. 287) • • •

"It has been held that a contract which requires the assignee to advance money for drilling implies a covenant to develop (Stanolind Oil Company *v.* Kimmel, 68 Fed. (2d) 520; Patsy Oil & Gas Company *v.* Baker, 259 P. 864). The same reasoning, we think, raises an implied covenant in this case where the duty was owed to the lessor and where *the only consideration moving to the assignor for a conveyance of minerals and of oil field equipment was an overriding royalty from the first oil produced* (emphasis supplied). Unless such an obligation be imposed, the conveyance is wholly without consideration. (R. 289) • • •

"Under any other holding the assignor, *his consideration consisting of royalty alone* (emphasis supplied), might be seriously prejudiced by deprivation of his only enforcement privilege." (R. 290)

It has been observed that the assignment recites a consideration of "$10.00 and other valuable considerations" and bears canceled revenue stamps in an amount aggregating $19.00. In 1934, revenue stamps were required on the basis of 50 cents for each $500.00 of consideration or fractional part thereof. Act Feb. 26, 1926, c. 27, Schedule (A) (8), as added by Act June 6, 1932, c. 209, § 725, 47 Stat. 275, and amended by Act June 16, 1933, c. 90, § 212, 48 Stat. 206. Thus, the inference is clear that approximately $19,000.00 was paid for the assignment.

Bearing strongly on this point is the following language appearing at page 125 of the Brief for Appellant filed in the Circuit Court of Appeals:

"For the sale and assignment by plaintiff, J. H. Gray, to defendant of the oil and gas lease in question, defendant paid said plaintiff a very substantial cash consideration, to which the $18,750, payable out of 1/4 of 7/8 of the first oil and gas produced and saved was additional. By the federal documentary stamps to the

assignment attached and canceled $19,000 is indicated to have been the cash consideration. It was as a matter of fact $18,750, which statement as a fact we do not anticipate will be disputed or a question raised thereon. As from our statement under this point apparent there was 37.5 acres in the lease. Defendant paid therefor at the rate of $500 per acre."

The appellee Gray did not deny the foregoing statements.

**Conclusion.**

It respectfully is submitted, therefore, that this case is one calling for the exercise of the supervisory powers of this court by granting a writ of certiorari and thereafter reviewing and reversing the decision of the Circuit Court of Appeals.

Respectfully submitted,

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